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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935.

No. 173

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE.

Petitioner,

vs.

SAMUEL A. SALVAGE,

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT.

JOHN G. JACKSON,
Attorney for Respondent,
SAMUEL A. SALVAGE.

WILLIAM H. WHITE, JR.,
GEORGE B. BROOKS,
of Counsel.

INDEX.

	PAGE
OPINIONS BELOW	1
JURISDICTION	1
QUESTIONS PRESENTED	2
STATUTES AND OTHER AUTHORITIES INVOLVED	2
STATEMENT	2
SUMMARY OF ARGUMENT	2
ARGUMENT	3
POINT I. Neither the question nor of recoupment is properly before the Court for consideration	3
POINT II. The Revenue Act itself precludes the Commissioner from claiming either estoppel or recoupment	6
POINT III. The Commissioner has failed to establish his claim of estoppel	7
POINT IV. Other cases cited by Commissioner to sustain his claim of estoppel	12
POINT V. A consideration of the case of *Bull* v. *United States*	17
CONCLUSION	18

CITATIONS.

CASES: PAGE

Adler v. *Commissioner*, 77 F. (2d) 733 14
Alice State Bank v. *Houston Pasture Co.*, 247 U. S. 240 5
Askin & Marine Co. v. *Commissioner*, 66 F. (2d) 776 14
Avery v. *Cleary*, 132 U. S. 604 11

Bothwell v. *Commissioner*, 77 Fed. (2d) 35 12
Bull v. *United States*, 295 U. S. 247 17
Burnet v. *Sanford & Brooks Co.*, 282 U. S. 359 17

Commissioner v. *Liberty Bank & Trust Co.*, 59 F. (2d) 320 14
Commissioner v. *Moore*, 48 F. (2d) 526 16
Continental Products Co. v. *Commissioner*, 66 F. (2d) 434 15
Crane v. *Commissioner*, 68 Fed. (2d) 640 ..... 12, 14
Clayton Magazines, Inc., In re, 77 Fed. (2d) 852 (C. C. A. 2nd Circuit) 18

Dickerson v. *Colgrove*, 100 U. S. 578 9
Dolan v. *Rodgers*, 149 N. Y. 489, 491; 44 N. E. 167 10
Duesenberg, Inc., 31 B. T. A. 922, 926 4

Giant Furniture Co. v. *United States*, 9 F. Supp. 585 14
Grouf v. *State National Bank*, 40 Fed. (2d) 2 4
Gunning v. *Cooley*, 281 U. S. 463 5

Haag v. *Commissioner*, 59 F. (2d) 514 14
Hartwell Mills v. *Rose*, 61 F. (2d) 441 15
Helvering v. *Brooklyn City R. Co.*, 72 Fed. (2d) 274 16
Helvering v. *General Utilities & Operating Co.*, 74 Fed. (2d) 972, 976 4
Helvering v. *Morgan's Inc.*, 293 U. S. 121 17

PAGE

Imperator Realty Co. v. *Tull*, 228 N. Y. 447, 457; 127 N. E. 263 11

Kirk v. *Hamilton*, 102 U. S. 68 9

Larkin v. *United States*, 78 Fed. (2d) 951 ..... 7, 13

Mahoning Investment Co. v. *United States*, 3 F. Supp. 622 14
Matern v. *Commissioner*, 61 F. (2d) 663..... 15
May Rogers, 31 B. T. A. 994 4
Merchants Heat & L. Co. v. *Clow*, 204 U. S. 286.... 4, 5
Moran v. *Commissioner*, 67 F. (2d) 601..... 16

Naumkeag Steam Cotton Co. v. *United States*, 2 F. Supp. 126 ..... 15, 16

Oklahoma v. *Texas*, 268 U. S. 252 9

Philadelphia, Wilmington & B. Ry. Co. v. *Howard*, 54 U. S. 307, 335 3

Stearns Co. v. *U. S.*, 291 U. S. 54 .....6, 9, 11, 15
Stone v. *Bank of Commerce*, 174 U. S. 412..... 8
Swartz v. *Commissioner*, 69 F. (2d) 633..... 14

The Viscose Company, 3 B. T. A. 444 8

United States v. *S. F. Scott & Sons*, 69 F. (2d) 728 16

Webster Co. v. *Splitdorf Co.*, 246 U. S. 463 5
West v. *Blakeway*, 2 Man. & G. 828, 839..... 10
Wheelock v. *Commissioner*, 77 F. (2d) 474..... 14

STATUTES:

Judicial Code, Section 240 (a) as amended 2
Revenue Act of 1928, Sections 607 and 609....2, 3, 6, 18

MISCELLANEOUS:

T. D. 3435, II-1, C. B. 50 13
L. O. 1095, I-1, C. B. 313 7

IN THE

SUPREME COURT OF THE UNITED STATES,

OCTOBER TERM—1935.

No. 173.

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,
against
SAMUEL A. SALVAGE.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT.

Opinions Below.

Memorandum opinion of Board of Tax Appeals (R., 2832) is unreported. The opinion of the Circuit Court of Appeals (R., 74-78) is reported in 76 Fed. (2d) 112.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered March 25, 1935 (R., 78). An order granting an extension of time thirty days from June 25, 1935, for filing a petition for certiorari was issued June 25, 1935 (R., 79).

The petition for a writ of certiorari was filed July 25, 1935, and granted October 14, 1935. The jurisdiction of this court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1935.

Questions Presented.

The claim of the Commissioner in this matter is that the taxpayer is estopped to claim a refund of taxes paid in 1929 by reason of his failure to include in his return for the year 1922 as taxable income the difference between the real value of stock of The Viscose Company received by him in that year and the amount in cash which he paid for the same. In his brief he also argues that even though the taxpayer is not so estopped nevertheless the Commissioner is entitled to recoupment against the taxpayer's claim.

Statutes and Other Authorities Involved.

The applicable statutes and other authorities involved are set forth in the appendix, pages 23 to 26, to the brief filed by the Commissioner herein. In addition, Section 607 and Section 609 (a) of the Revenue Act of 1928 are involved.

Statement.

The essential facts are set forth in the brief filed by the Commissioner herein and the briefs of the Commissioner and the taxpayer in Samuel A. Salvage, petitioner, against Guy T. Helvering, Commissioner of Internal Revenue, No. 280.

Summary of Argument.

The taxpayer contends in this case, first, that neither the claim of estoppel nor of recoupment is available to the Commissioner by reason of the fact that he failed to plead

the same as affirmative defenses; second, that the provisions of Sections 607 and 609 (a) of the Revenue Act of 1928 preclude him from succeeding in such claims; and, third, that even though said defenses were available the facts in the record do not sustain the Commissioner's contentions, he having failed to prove the elements necessary to establish estoppel or recoupment.

Argument.

At the outset we submit two points which we believe are sufficient to dispose of the Commissioner's contentions, without further consideration of the cases cited by him in support thereof.

POINT I.

Neither the question of estoppel nor of recoupment is properly before the Court for consideration.

In our main brief we have stated reasons and authorities which we believe support this contention. In addition to the authorities there cited to support the claim that Rule 14 of the Board of Tax Appeals is clear and explicit in its provisions and that the Board itself has construed it to require the pleading of estoppel as an affirmative defense, we submit the following:

In *Philadelphia, Wilmington & B. Ry. Co.* v. *Howard*, 54 U. S. 307, 335, the court says:

> "If a party has opportunity to plead an estoppel and voluntarily omits to do so and tenders or takes issue on the facts, he thus waives the estoppel and commits the matter to the jury who are to find the truth."

In the instant case the Commissioner was fully advised of the nature of the taxpayer's claim by his petition to the Board of Tax Appeals and had full opportunity to plead thereto.

In *Northport Shores Inc.*, 31 B. T. A. 1013, 1018, the Board stated:

> "Since estoppel is an affirmative defense respondent must prove all of its essential elements are present."

In *Duesenberg Inc.*, 31 B. T. A. 922, 926, the Board states:

> "But estoppel is a defense which must be pleaded and proved and since it was neither pleaded nor proved in the present case it deserves no further consideration."

In *May Rogers*, 31 B. T. A. 994, the Board says, referring to estoppel, at page 1004:

> "Aside from these considerations the answers of the respondent allege no facts on the question as required by Rule 14 of the Board's rules of practice. Beyond statements made by his counsel at the hearing he has not raised the issue." (Citing cases.)

See also *Grauf* v. *State National Bank*, 40 Fed. (2d) 2.

The requirement that an affirmative defense must be pleaded is not a mere technicality but is founded in reason. Without the plea the opponent has no opportunity to resist the new issue by amendment of the pleadings or by additional proof. *Helvering* v. *General Utilities & Operating Co.*, 74 Fed. (2d) 972, 976.

In connection with the claim now for the first time made by the Commissioner that he is entitled to recoupment the same reasoning applies. Recoupment is an affirmative defense. See *Merchants Heat & L. Co.* v. *Clow*, 204 U. S. 286. Reference is also made to Equity Rule 30.

An additional reason for not considering the plea of recoupment lies in the fact that the one error assigned by

the Commissioner in his application for a writ makes no reference whatsoever to this claim. This court will ordinarily not consider questions not certified to it. See *Alice State Bank* v. *Houston Pasture Co.*, 247 U. S. 240; *Webster Co.* v. *Splitdorf Co.*, 264 U. S. 463; *Gunning* v. *Cooley*, 281 U. S. 90.

In his brief the Commissioner relies on *Helvering* v. *General Utilities & Operating Co.*, supra, as authority for the proposition that estoppel was not required to be pleaded. This case is in fact authority to the contrary. No question of estoppel was involved and the only question was one of law as to the proper basis of computing tax liabilities from stipulated facts. The court says:

> "The reason for the rule, sometimes enforced by the courts, that an appellate court will confine itself to the issue presented and ruled upon by the court below, is based on the ground that the opposing party has no opportunity to resist the new issue by amendment of the pleadings or by additional proof. No such conditions exist here. No amendment to the pleadings is required to settle the issue here discussed, and no additional evidence could change the stipulated fact."

In the case now before the court a plea either of estoppel or recoupment would have permitted the taxpayer to establish whether or not the necessary elements thereof were present.

The question of lack of proof of estoppel we believe is sufficiently covered in our main brief. The reasoning in connection therewith applies even more strongly to the claim of recoupment. Recoupment is a cross demand seeking a credit against plaintiff's claim. Absolutely no proof has been presented as to the amount for which credit is claimed and there is no evidence in the record by which any Court could arrive at any figure.

POINT II.

The Revenue Act itself precludes the Commissioner from claiming either estoppel or recoupment.

Section 607 and Section 609 (a) of the Revenue Act of 1928 read as follows:

> "Sec. 607. (Revenue Act of 1928). Any tax (or any interest, penalty, additional amount, or addition to such tax) assessed or paid (whether before or after the enactment of this Act) after the expiration of the period of limitation properly applicable thereto shall be considered an overpayment and shall be credited or refunded to the taxpayer if claim therefor is filed within the period of limitation for filing such claim."
>
> "Sec. 609. (Revenue Act of 1928). (a) Credit against barred deficiency.—Any credit against a liability in respect of any taxable year shall be void if any payment in respect of such liability would be considered an overpayment under section 607."

A reading of these sections shows that it was the clear intention of the Legislature that once a claim was barred by the statute the amount thereof could not be used by the Commissioner to offset an overpayment made in a subsequent year. The only modification that can be found in respect to this rule is in *Stearns Co.* v. *U. S.*, 291 U. S. 54, at page 60, where the court says:

> "The aim of that provision, as we view it, was to invalidate such a credit if made by the Commissioner of his own motion without the taxpayer's approval or with an approval falling short of inducement or request."

Certainly here there are no facts upon which to base a claim of such inducement or request. As a practical matter, under the construction given to these sections by the courts, if this taxpayer today paid a tax on his 1922 income

based upon the item in controversy (assuming any such tax would have been due) he could forthwith file a claim for and obtain a refund of the entire amount so paid.

See also L. O. 1095, I-1 C. B. 313.

The statute is in effect nullified if the claims of the Commissioner are allowed.

POINT III.

The Commissioner has failed to establish his claim of estoppel.

The Commissioner rests his case on the claim that it was the taxpayer's duty to report as income in his 1922 return the difference between the cash cost of the shares of the old company and their fair market value; that his failure to so report constituted a representation to the Commissioner that no income had been received; that the Commissioner relied upon that representation to the Government's detriment—by reason of all of which the taxpayer may not now have his tax liability computed as prescribed by the Revenue Law in effect in that year but must accept some other basis of value fixed in accordance with a theory advanced by the Commissioner.

To support this claim the taxpayer is charged with "omission, concealment or wrongdoing" (p. 12, Commissioner's Brief), although it is admitted his return was made on the basis of an ordinary stock purchase which was the basis of all income tax returns of so-called bargain purchases prior to the announcement of Treasury Decision 3435 in February, 1923, more than a month after the stock purchase (Commissioner's Brief, p. 26), and although counsel for the Commissioner cites *Larkin* v. *United States* (78 Fed. (2d) 951), as holding that this Treasury Decision was only prospective in its operation and, hence, not applicable

to a purchase of stock in 1922. Inasmuch as a Treasury Decision is not legislation but simply an interpretation of existing law, we respectfully doubt the correctness of the holding in the *Larkin* case and refer to these matters only as showing that no basis exists for a charge against the taxpayer implying anything beyond an innocent omission from his 1922 return. Indeed the Circuit Court suggested that the failure to report might be due to an innocent mistake of law (R., p. 76).

In 1929 when the taxpayer was confronted with the problem of determining how much of the proceeds derived from the redemption of the American Viscose Corporation preferred stock was subject to income tax, for the reasons reviewed in our main brief and believing an apportionment was not practicable he made his return on that basis. In so doing he was supported by a decision of the Board of Tax Appeals (*The Viscose Company*, 3 B. T. A. 444) and he is not, we submit, subject to criticism for heeding the decision of the Board rather than an informal memorandum prepared by his accountants.

Mr. Salvage was at all times entirely willing that his tax liability should be determined on the basis of his returns as made and vigorously contended for such determination before the Board and the Circuit Court. It is the Commissioner who has driven him from that position and it is the Commissioner who is asserting that tax liability shall be determined on a basis other than that prescribed by the Revenue Law. It is the Commissioner, and not the taxpayer, who is seeking to make ineffective the Statute of Limitations and substitute therefor an expansion of the doctrine of equitable estoppel unsupported by any decision of this Court.

The Commissioner cites four cases in this Court in support of his contention (page 11) that the taxpayer's failure to report the income constituted in effect a representation to the Commissioner that no income had been received.

Stone v. *Bank of Commerce*, 174 U. S. 412, is a case in which the bank sought to estop the collection of certain

taxes by the State on the ground that the attorney for a collector had agreed that it would be taxed under a certain Act and that it could not be taxed under a subsequent Act. No damage was shown. The court held that no estoppel could properly be urged. The case is absolutely no authority for the Commissioner's contention.

In *Kirk* v. *Hamilton*, 102 U. S. 68, and *Dickerson* v. *Colgrove*, 100 U. S. 578, land was conveyed by persons having no legal right to give title. The respective true owners knew of the conveyances and in the first case remained silent while the land was improved and in the second affirmatively stated that the title would not be attacked. The court in each instance held that the conduct was such that they could not in equity change their positions. These cases obviously have no bearing here.

Oklahoma v. *Texas*, 268 U. S. 252, is authority, if anything, for the taxpayer. The court at page 257 says:

> "Only where conduct or statements are calculated to mislead a party and are acted upon by him in good faith to his prejudice can he invoke them as a basis of such an estoppel. And if they relate to the title of real property 'where the condition of the title is known to both parties, or both have the same means of ascertaining the truth, there can be no estoppel.'"

Stearns Company v. *United States, supra*, is the authority upon which the Commissioner apparently chiefly relies. In that case the taxpayer's returns for 1917 and 1918 were audited by the Commissioner. In June, 1923, the Commissioner made an additional assessment for the year 1917 of some $20,000., payment of which was demanded on August 3rd, 1923. On August 9th the taxpayer filed a claim for refund and credit of taxes alleged to have been overpaid for the years 1918, 1919, 1920 and 1921 amounting in the aggregate to over $35,000., and asked that the unpaid balance for 1917 be set off against the claim for overpayment and that the remainder be refunded. In June,

1924, the Commissioner allowed the claim of overassessment for 1918 in the sum of about $15,000. This overassessment was applied as a credit against the additional taxes due for 1917, leaving a balance of some $5,800. due the Collector which was on demand paid by the taxpayer without protest of any kind. Some six years later the taxpayer sued to recover the amount so credited, claiming that the Commissioner had been barred by the Statute of Limitations from making the additional assessment of 1917 taxes and, hence, the credit was improperly applied against that liability and should be refunded. Aside from a question as to the legality and effectiveness of a waiver of the statute signed by the taxpayer, the Court said with respect to the request to withhold the process of collection until credits were adjusted which the petitioner had filed with the Commissioner in August, 1923:

> "In substance the request was this: Please do not collect the tax for 1917, until you have completed the audit for the years 1918 to 1921 inclusive, and if there has been overassessment for those years, set it off as a credit" (p. 60).

The Court held that this amounted to something more than a waiver.

> "there was a positive request, which till revoked upon reasonable notice had the effect of an estoppel" (p. 59).
>
> * * * * * * *
>
> "The applicable principle is fundamental and unquestioned. 'He who prevents a thing from being done may not avail himself of the non-performance which he has himself occasioned, for the law says to him in effect "This is your own act, and therefore you are not damnified."' *Dolan* v. *Rodgers*, 149 N. Y. 489, 491; 44 N. E. 167; and *Imperator Realty Co.* v. *Tull*, 228 N. Y. 447, 457; 127 N. E. 263; quoting *West* v. *Blakeway*, 2 Man. & G. 828, 839. Sometimes the resulting disability has been characterized as an estoppel, sometimes as a waiver. The label counts

> for little. Enough for present purposes that the disability has its roots in a principle more nearly ultimate than either waiver or estoppel, the principle that no one shall be permitted to found any claim upon his own inequity or take advantage of his own wrong. *Imperator Realty Co.* v. *Tull*, supra. A suit may not be built on an omission induced by him who sues. * * * " (p. 61).

The foregoing case so differs from the case before the Court as to constitute no precedent. In the *Stearns Company* case the Commissioner received from and relied upon the "positive request" of the taxpayer, which induced the Commissioner not to act as he would have except for the request. The Court held the taxpayer's conduct to be inequitable and wrongful—thus completing the definition of an equitable estoppel, for the element of damage to the Commissioner was definitely established.

In the case before the court we believe the record clearly shows that the Commissioner's conduct in omitting to assess was not consequent upon any "positive request" or other inducement by the taxpayer, that the conduct of the taxpayer, which we have reviewed, was neither inequitable nor wrongful and that there is no evidence of damage to the Commissioner.

Avery v. *Cleary*, 132 U. S. 604, presents a close analogy. There a bankrupt omitted from his schedules and failed to disclose to the assignee in bankruptcy the existence of policies of insurance on the bankrupt's life. The bankrupt died and the proceeds of the policies were collected by the administrator of the bankrupt's estate for the benefit of his two daughters. The assignee in bankruptcy sued the administrator to collect the proceeds of the policies and the administrator pleaded that the suit was barred by the Statute of Limitations. The Court held with the administrator, saying (p. 610):

> "If it be assumed that Ellis had not, prior to his bankruptcy, delivered the assignment of May 19, 1877, and that his interests and rights in these poli-

cies were transferable to his assignee, the mere fact that he omitted any mention of the policies in his schedules in bankruptcy, and that neither he nor his administrator gave information of them to the assignee, would not establish fraud within the meaning of the rule announced in *Bailey* v. *Glover*. The omission from the schedules of any reference to the policies, and the failure to call the attention of the assignee to them, may have been caused by an honest belief, upon the part of Ellis, that they belonged to his children, or were not such property as the law required to be surrendered to the assignee; and, therefore, he lodged the assignment to Morse—possibly after his bankruptcy—with the insurance company."

The present case even more strongly negatives any wrongdoing, for it is clear that the taxpayer acted throughout in entire good faith.

POINT IV.

Other cases cited by Commissioner to sustain his claim of estoppel.

In our main brief we have set forth the reasons why estoppel cannot be applied in this case under the general definitions, rules and precedents dealing with that defense. In this point we will confine ourselves to distinguishing the cases decided by the lower courts which are cited by the Commissioner in support of his contention.

The Commissioner (page 12) states that there are two cases in which the facts were almost identical with the facts in the case at bar, namely, *Bothwell* v. *Commissioner*, 77 Fed. (2d) 35, and *Larkin, et al.* v. *United States*, 78 Fed. (2d) 951. He also states that the case of *Crane* v. *Commissioner*, 68 Fed. (2d) 640, was a case similar in all respects.

In the *Bothwell* case, petitioners in 1922 received an option to purchase certain stock at $2.00 per share, which

was exercised in 1927, and the stock was sold in 1928 at a substantial profit. In their returns the petitioners returned the profit as a capital net gain. The Commissioner ruled that it was ordinary gain. Petitions were filed on the basis of the returns but subsequently, and after the statute had run against the year 1927, the petitions were amended to include a claim that the difference represented compensation for services in 1927. The Commissioner pleaded estoppel among other things. The Court held that compensation had not in fact been received but that in any event inasmuch as the taxpayers had *affirmatively asserted* in their returns and continued to assert until after the statute had run that the whole of the profit derived was capital gain they could not repudiate their position.

The case is clearly distinguishable in that (1) estoppel was pleaded; (2) the holding in respect to estoppel was not necessary to the decision; and (3) the petitions filed constituted positive assertions as to the legal position taken by petitioners and the Commissioner was entitled to rely upon these.

In the case of *Larkin et al.* v. *United States*, the opinion does not give sufficient information to determine whether or not the taxpayers, at the time they acquired the stock in question, should have known that the difference in value constituted taxable income. It does state that they were permitted to buy the stock "by reason of their long and faithful service." The case was in fact determined by the court upon the theory that T. D. 3435 II-1, C. B. 50, had not been promulgated at the time the stock was acquired, was not retroactive in effect and therefore that the difference in value did not in fact constitute taxable gain at that time. The language in respect to estoppel was not necessary to the decision. Moreover in the *Larkin* case the proceeding was initiated by the taxpayer; in the case before the Court the taxpayer has shifted his position under compulsion and solely by way of defense. While it is our view that the decision in this case was incorrect, nevertheless we submit that the above facts distinguish it.

Crane v. *Commissioner*. Contrary to the statement made at page 21 of the Commissioner's brief, the Board of Tax Appeals did not consider the question of estoppel, as a study of the record and of the opinion, 27 B. T. A. 360, shows. The Board decided the case solely on a question of statutory construction. In the Circuit Court of Appeals, although certain language indicates that the court had in mind estoppel, or something in the nature thereof, nevertheless the opinion does not use the word and in fact a careful study indicates that the Court also passed on the matter from the point of view of statutory construction. At page 641 the Court states:

> "It may be doubted whether the foregoing statutes and regulations require such a construction in all cases."

and further

> "The statutes and regulation should not be construed to entitle a taxpayer to the benefit of an expenditure made by his lessee, when the taxpayer has failed to report or to pay a tax in the appropriate year. * * *"

The concurring opinion of Judge Morton rejects the theory that failure to report income, however innocent, constituted a statement that no such income was received.

The Commissioner's brief cites a number of other cases as supporting his position without any analysis of the facts. A study of these cases shows that they are distinguishable from the case before the Court. In a number of them there was a positive and affirmative assertion contained either in the return involved or some other return, which assertion the taxpayer subsequently endeavored to repudiate. This is true of the cases of *Wheelock* v. *Commissioner*, 77 F. (2d) 474; *Haas* v. *Commissioner*, 59 F. (2d) 514; *Askin & Marine Co.* v. *Commissioner*, 66 F. (2d) 776; *Commissioner* v. *Liberty Bank & Trust Co.*, 59 F. (2d) 329; *Giant Furniture Co.* v. *United States*, 9 F. Supp. 585; *Swartz* v. *Commissioner*, 69 F. (2d) 633; *Adler* v. *Commissioner*, 77 F. (2d) 733; *Mahoning Investment Co.* v. *United States*,

3 F. Supp. 622; and *Matern* v. *Commissioner*, 61 F. (2d) 663.

The case of *Continental Products Co.* v. *Commissioner*, 66 F. (2d) 434, is similar to the *Bothwell* case. In that case the taxpayer filed a petition to the Board of Tax Appeals based upon a letter from the Commissioner which it stated was a deficiency letter, the filing of the petition of course staying the collection of any tax. After the statute had run it reversed its position and claimed that the letter did not constitute a deficiency letter and that the Commissioner's claim for tax was barred. It was held that the filing of the petition constituted an affirmative assertion by which the taxpayer was bound.

A similar case is *Hartwell Mills* v. *Rose*, 68 F. (2d) 441, where the taxpayer sought to recover an overpayment after the limitation period but had filed a claim for abatement which took it out of the operation of Section 607 of the Revenue Act. Subsequently he endeavored to argue that the claim for abatement was not legally filed and the Court held that he was precluded from urging this claim, saying that where the Government and the taxpayer by acquiescing in the manner of performing an act had given a definite character and effect to it, the taxpayer will not be permitted, after deriving benefits from its acquiescence, to deny its character or to change his position at the Government's expense.

The case of *Naumkeag Steam Cotton Co.* v. *United States*, 2 F. Supp. 126, is similar to the case of *Stearns Co.* v. *United States, supra*, in that it involves a positive request by the taxpayer to the Commissioner upon which the latter acted.

In all of the cases above cited the courts have made an effort to meet the requirements of equitable estoppel, to wit, intentional representation or inducement, reliance and damage. Either the representation or inducement has been found in an affirmative assertion contained either in a formal claim, the return or, as in the *Naumkeag* case, a direct request. In none of these cases has it been held that innocent omission of an item from the return constituted a representation upon which estoppel could be predicated. While

we do not concede that these cases are sound even on their own facts, nevertheless we believe that they are so distinguishable as to have no application in this case.

The cases of *Commissioner* v. *Moore,* 48 F. (2d) 526 and *Moran* v. *Commissioner,* 67 F. (2d) 601, are cases where the taxpayer adopted a certain theory of accounting, having or believing he had the option to treat income as having been received in one or more of several years. The effect of the decisions is simply that the taxpayer had made an election by which he was bound. It is to be noted that the Court in the *Crane* case used language indicating that they regarded the situation as similar, and indeed Judge Morton's concurring opinion specifically goes upon that ground, citing the *Moran* case.

The Commissioner endeavors to distinguish the cases of *United States* v. *S. F. Scott & Sons,* 69 F. (2d) 728, and *Helvering* v. *Brooklyn City R. Co.,* 72 Fed. (2d) 274. In respect to the *Scott* case, there is nothing in the record here to indicate that the Commissioner was not fully advised of the situation at the time of the audit of the 1922 return or in any event before the statute had run. The taxpayer returned the dividends on the stock and the Commissioner could, and presumably did, investigate both his records and the records of the corporation. *The Brooklyn City R. Co.* case, we submit is particularly applicable. Judge Hand there said:

> "The Commissioner argues that the opportunity to reassess the income both before and after 1921 has long since expired, and that he has lost this right because he relied upon the return as filed. This he must prove, for estoppel is an affirmative defense. In the first place it does not appear that he did not have immediate access to all the books of the taxpayer in every year in which a return was filed; he may have actually examined them. Therefore the record does not establish an estoppel * * *"

The Commissioner argues that in that case a cursory examination of taxpayer's books would have disclosed the error and that it was not shown that the tax for earlier years would have been greater. Both of these statements apply directly to this case.

POINT V.

A consideration of the case of Bull v. United States.

This court has not had occasion, so far as we have been able to ascertain, to consider the effect of the *Bull* case on other states of facts since that decision was rendered, and we, therefore, confine ourselves to pointing out the distinctions which exist between the respective states of facts and to what seems to us the logical application of the decision to this case in view of the general rules of law and other decisions of this court.

In the *Bull* case claim was made by the taxpayer, while here it is made by the Commissioner; there, there was an identical sum of money which was doubly taxed, while here there are two different items involved; there one tax year was involved, while here there are two different tax years; there the Government had actually received a sum of money while here the taxpayer has received nothing.

Since the Sixteenth Amendment was passed, income taxes have been consistently assessed on the basis of annual accounting periods, which periods have been known as taxable years, and the provisions of the taxing statutes have been drafted and enacted with primary reference to such normal accounting periods. *Helvering* v. *Morgan's Inc.*, 293 U. S. 121, *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359. Each year is governed by the particular Revenue Act applicable thereto, which defines income, both gross and net, and prescribes the rates of taxation. The taxpayer has the obligation to file a return and pay a tax for the annual period and the Collector has the right of collection. Thus the legal rights of the parties are fixed separately for each annual period and the whole scheme of the revenue acts has been to regulate the several tax periods as constituting different transactions between the parties.

To hold otherwise would necessitate proceeding upon the assumption that there is a continuous running account,

between the taxpayer and the government which permits a reopening of all past years—by the government in the event of a claim for refund and by the taxpayer in the event of a deficiency. That this was not the intent seems to us to be demonstrated by the terms of Section 607 and Section 609 of the Revenue Act of 1928, *supra*.

In the case of *In re Clayton Magazines, Inc.*, 77 Fed. (2d) 852 (C. C. A. 2nd Circuit), the court held the taxpayer could not offset a claim for refund against which the statute had run against a claim on the part of the Commissioner for additional taxes for a different year. We submit the distinction made by that court is sound.

So far as the claim might be made that the income here involved is in both years part of the same transaction or related to the same transaction, we point out that practically all profits arise from the investment or reinvestment of earned income and the interest and dividends received thereon, and almost any transaction relating to the disposition of property and taxation of the profits arising therefrom taking place in one year could be in some way related to transactions of previous years by tracing the source of the property back to the point when it came into the hands of the taxpayer either in the same or a different form.

Conclusion.

It is therefore respectfully submitted that the decision of the court below should be affirmed in so far as it denies to the Commissioner the judgment for any deficiency and should be affirmed in so far as it allows to the taxpayer a refund and should be modified so as to allow to the taxpayer his full refund claimed of $63,750.

JOHN G. JACKSON,
Attorney for Respondent,
SAMUEL A. SALVAGE.

WILLIAM H. WHITE, JR.
GEORGE B. BROOKS
of Counsel.